

Message Text

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ACTION AF-10

INFO OCT-01 EUR-12 IO-13 ISO-00 AID-05 CIAE-00 COME-00

EB-08 FRB-03 INR-10 NSAE-00 USIA-06 TRSE-00

XMB-02 OPIC-03 SP-02 LAB-04 SIL-01 OMB-01 DODE-00

PM-05 H-01 L-03 NSC-05 PA-01 SS-15 CEA-01 STR-07

/119 W

-----081672 222001Z /45

R 220735Z MAR 78

FM AMEMBASSY PRETORIA

TO SECSTATE WASHDC 792

INFO AMCONSUL CAPE TOWN

USMISSION GENEVA

AMEMBASSY LONDON

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CAPE TOWN ALSO FOR EMBASSY

E.O. 11652: N/A

TAGS: EGEN, EFIN, SF

SUBJECT: SOUTH AFRICAN ECONOMIC MOOD REMAINS PESSIMISTIC ON

EVE OF BUDGET

SUMMARY: WITH PRESENTATION OF FY 78/79 BUDGET LESS THAN TWO WEEKS AWAY, PRIVATE SECTOR ECONOMISTS ARE TAKING AN INCREASINGLY PESSIMISTIC TONE IN BOTH PUBLIC AND PRIVATE STATEMENTS ON PROSPECTS FOR 1978. PUBLIC STATEMENTS REFLECT IN PART AN EFFORT TO PUSH THE SAG TOWARD A MORE EXPANSIONARY FISCAL POLICY AS MANY ECONOMISTS ARE QUESTIONING WHETHER 1978 WILL IN FACT SEE EVEN A MODERATE RECOVERY WITHOUT MORE GOVERNMENT STIMULATION. ECONOMISTS OF TWO LEADING BANKS HAVE CALLED FOR DIRECT CONTROLS IN IMPORTS TO ALLOW RECOVERY WITHOUT HARMING BALANCE OF PAYMENTS. "FINANCIAL MAIL" BELIEVES RAND DEVALUATION WOULD SERVE SAME PURPOSE, BUT THIS HAS BEEN REJECTED BY MINISTER OF FINANCE HORWOOD. END SUMMARY

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1. JOHANN CLOETE, CHIEF ECONOMIST OF BARCLAYS BANK AND WELL KNOWN MONETARIST, HAS STATED THERE IS LITTLE HOPE FOR A RECOVERY UNLESS THE GOVERNMENT IS WILLING TO ALLOW A SIGNIFICANTLY GREATER INCREASE IN THE MONEY SUPPLY THAN THE ESTIMATED 7 PER CENT GROWTH IN 1977 (A NEGATIVE GROWTH IN REAL TERMS). HE BELIEVES THAT A 13 PER CENT GROWTH IN MONEY SUPPLY WILL NOT PRODUCE EXCESSIVE PRESSURES ON IMPORTS AND BALANCE OF PAYMENTS IN VIEW OF THE LARGE

EXCESS INDUSTRIAL CAPACITY NOW AVAILABLE. IF IMPORTS SHOULD BECOME A PROBLEM UNDER AN EXPANSIONARY POLICY, CLOETE HAS CALLED FOR DIRECT IMPORT CONTROLS.

2. RAYMOND PARSONS, OF THE ASSOCIATION OF CHAMBERS OF COMMERCE, STATED IN RECENT SPEECH THAT BUSINESS MOOD IS STILL BASICALLY PESSIMISTIC, AND BUSINESSMEN ARE DISILLUSIONED AT FAILURE OF RECOVERY TO MATERIALIZE. FURTHER GOVERNMENT STIMULATION IS NOW REQUIRED ACCORDING TO PARSONS AND WITHOUT IT THERE IS A REAL CHANCE THAT GROWTH IN 1978 WILL BE LESS THAN 2 PER CENT (COMPARED TO AN ESTIMATED 1 PERCENT IN 1977).

3. IN CONTRAST, ANDRE HAMMERSMA, CHIEF ECONOMIST FOR STANDARD BANK, TOLD EMBOFF THAT HE DOES NOT SEE BUDGET AS HAVING CAPABILITY TO SIGNIFICANTLY INFLUENCE ECONOMY AS ADDITIONAL AMOUNTS GOVERNMENT CAN REALISTICALLY SPEND ARE TOO SMALL. HAMMERSMA NOTED THAT WHILE RISE IN CAR SALES AND IMPORTS ARE SLIGHT POSITIVE SIGNS, DEMAND FOR BANK LOANS CONTINUES TO BE WEAK. BUSINESS CONFIDENCE REMAINS LOW AND THREAT OF SANCTIONS BECOMING INCREASINGLY SERIOUS FACTOR WHICH MAY NECESSITATE ADJUSTMENTS IN ECONOMY. BEST THAT CAN BE HOPED FOR IS WEAK REVIVAL STRETCHING OVER A PERIOD OF YEARS. IMPORT SUBSTITUTION ACCORDING TO HAMMERSMA IS ONLY ELEMENT ON HORIZON THAT WOULD GIVE A BIT OF STIMULUS WITH SANCTIONS THREAT MAKING THIS SOMETHING GOVERNMENT SHOULD MORE ACTIVELY ENCOURAGE. HAMMERSMA BELIEVES THAT IN CURRENT CIRCUMSTANCES, SOUTH AFRICA CANNOT CONTINUE ITS TRADITIONAL LIBERAL TRADE LIMITED OFFICIAL USE

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POLICIES AND RELY ON EXPORTS TO PULL THE ECONOMY OUT OF RECESSION. CONTROLS ON IMPORTS ARE NEEDED EVEN IF THIS MEANS ABANDONING GATT COMMITMENTS. EMPLOYMENT AND ECONOMIC RECOVERY MUST TAKE FIRST PRECEDENCE ACCORDING TO HAMMERSMA.

4. STELLENBOSCH BUREAU OF ECONOMIC RESEARCH (BER) REPORTS THAT ITS SET OF COINCIDING ECONOMIC INDICATORS SHOW THAT ECONOMY HAS NOW LEVELED OUT AFTER LONG DECLINE BUT THAT UPWARD MOVEMENT IS STILL SO WEAK AS TO BE IMPERCEPTIBLE. BER ALSO REPORTS THAT CONSUMER CONFIDENCE DECLINED IN FINAL QUARTER OF 1977 DUE TO POLITICAL EVENTS DURING PERIOD.

5. THE "FINANCIAL MAIL" HAS PROPOSED THAT SAG ACT AGAINST CURRENT STAGNATION BY PROGRAM OF FISCAL STIMULATION AND, IN ORDER TO SIMULTANEOUSLY PROTECT THE BALANCE OF PAYMENTS PROPOSES A DEVALUATION OF THE RAND FOLLOWED BY A FLOAT. MAIL, HOWEVER, HAS LITTLE SUPPORT IN PROPOSING DEVALUATION. HAMMERSMA POINTS OUT WEAKER RAND WOULD CAUSE FURTHER STRAINS FOR BUSINESSES HAVING TO REPAY PREVIOUS FOREIGN LOANS AND WOULD ENCOURAGE SPECULATION AGAINST RAND. THE RAND, BEING PEGGED TO THE DOLLAR, HAS LOST 7.6 PER CENT OF ITS VALUE IN LAST SIX MONTHS AGAINST WEIGHTED AVERAGE OF CURRENCIES OF SOUTH AFRICAN TRADING PARTNERS

ACCORDING TO BARCLAY BANK STUDY. MINISTER OF FINANCE HORWOOD STATED IN A MARCH 10 SPEECH THAT THIS DECLINE "HAS FITTED RATHER WELL INTO OFFICIAL ECONOMIC POLICY" AND THERE IS NO REASON TO EITHER DEVALUE OR REVALUE AT THIS TIME.

6. RECENT PROVISIONAL ESTIMATES OF GOVERNMENT SPENDING SUGGEST SAG MAY HAVE MORE FLEXIBILITY TO EITHER INCREASE SPENDING OR CUT TAXES THAN WAS PREVIOUSLY BELIEVED. ESTIMATES FOR 11-MONTH PERIOD TO END OF FEBRUARY SHOW GOVERNMENT SPENDING AS R7,822 COMPARED TO BUDGET LEVEL FOR ALL OF FY 77/78 OF R8,775 MILLION. DEFENSE EXPENDITURES ARE PROVISIONALLY REPORTED TO AMOUNT TO ONLY R1,270 MILLION IN 11-MONTH PERIOD AS OPPOSED TO BUDGETED ANNUAL FIGURE OF R1,654 MILLION. ARMS EMBARGO IS BELIEVED A MAJOR FACTOR IN THIS SHORTFALL. "RAND DAILY MAIL" ESTIMATES SAG WILL BE OVERALL LIMITED OFFICIAL USE

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R300-400 MILLION UNDERSPENT IN CURRENT FISCAL YEAR ENDING MARCH 31. GOVERNMENT INCOME IS ALSO EXPECTED TO BE DOWN DUE TO RECESSION, BUT SAG HAS NO REAL DIFFICULTY IN RAISING LOANS ON LIQUID DOMESTIC MARKET. A REDUCTION OF INDIVIDUAL INCOME TAXES WOULD BE QUITE ATTRACTIVE BECAUSE AFTER TAX INCOMES OF WHITES HAVE BEEN DECLINING IN REAL TERMS FOR LAST THREE YEARS.

7. COMMENT: IN CYCLICAL TERMS, SOUTH AFRICAN ECONOMY IS OVERDUE FOR RECOVERY. HOWEVER, POLITICAL FACTORS ARE HAVING SUCH A LARGE IMPACT OF BUSINESS CONFIDENCE THAT AN EXPANSIONARY GOVERNMENT FISCAL POLICY AND ITS ATTENDANT PSYCHOLOGICAL BOOST MAY BE ONLY WAY EVEN EARLIER MODEST GROWTH PROJECTIONS OF 3 PER CENT CAN BE MET IN 1978. THE QUESTION WOULD THEN ARISE HOW TO PROTECT THE BALANCE OF PAYMENTS. CLOETE AND OTHERS FEEL THAT BALANCE OF PAYMENTS PRESSURE WOULD BE SUPPORTABLE AND CONTINUATION OF CURRENT RECESSION POSES GREATER DANGER. IF THIS DID NOT PROVE TO BE THE CASE, IMPORT CONTROLS WOULD LOOK VERY ATTRACTIVE TO SAG. RESERVE BANK IS KNOWN, HOWEVER, TO BE STRONGLY OPPOSED TO A SIGNIFICANTLY MORE EXPANSIONARY COURSE.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: GOVERNMENT BUDGET, ECONOMIC PROGRAMS
Control Number: n/a
Copy: SINGLE
Draft Date: 22 mar 1978
Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978PRETOR01641
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D780126-0870
Format: TEL
From: PRETORIA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780337/aaaabfeh.tel
Line Count: 156
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 6e5ac1bf-c288-dd11-92da-001cc4696bcc
Office: ACTION AF
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 19 apr 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3238582
Secure: OPEN
Status: NATIVE
Subject: SOUTH AFRICAN ECONOMIC MOOD REMAINS PESSIMISTIC ON EVE OF BUDGET SUMMARY: WITH PRESENTATION OF FY 78/79
BUDGET LES
TAGS: EGEN, EFIN, PGOV, SF
To: STATE
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/6e5ac1bf-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014